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yangarra resources ltd.

2005 Annual Report

CORPORATE PROFILE

Yangarra Resources Ltd. is a junior oil and gas company focused on the exploration, development and production of natural gas and oil with operations in Western Canada. Yangarra Resources Ltd. was formed on November 9th, 2005 pursuant to a merger of Yangarra Resources Inc. and TriOil Ltd. The corporation's strategy is to increase the value of its corporate assets through the drill bit and by assembling a large land base in Alberta that features high-quality, long life gas reserves.

Yangarra trades on the TSX Venture Exchange under the symbol "YAN".

ANNUAL MEETING

The Annual General Meeting of Shareholders of Yangarra Resources Ltd. will be held on July 25th, 2006 at 3:00 p.m. at Suite #1600, 333 - 7 Avenue S.W. Calgary, Alberta.
Shareholders and others interested in the business of the Company are welcome to attend.

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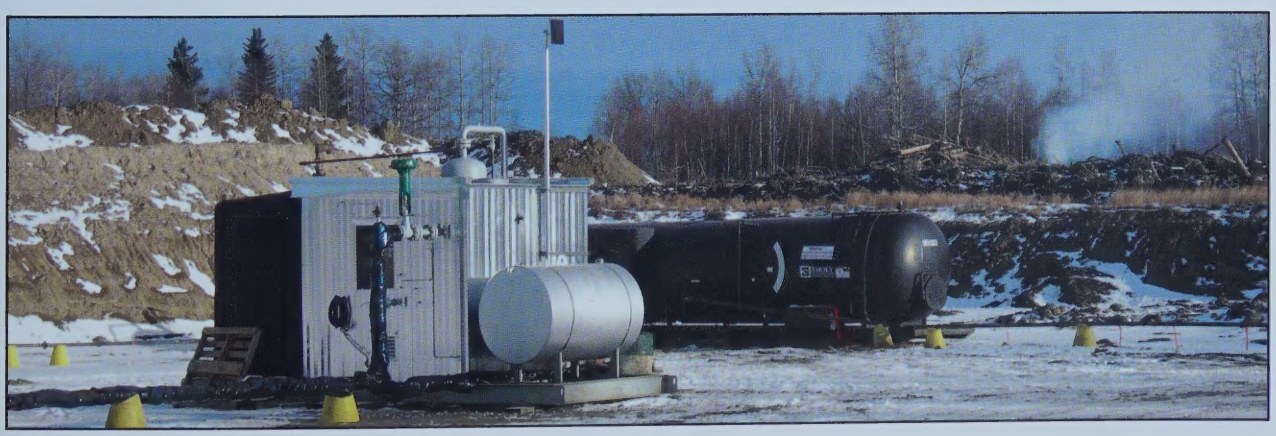
Forward-looking statements: This document contains forward-looking statements. The reader should be aware that historical results are not necessarily indicative of future performance. Forward looking statements are based on current expectations that involve a number of risks and uncertainties that could cause actual events or results to differ materially from those reflected herein.



PRESIDENT'S MESSAGE

TO OUR SHAREHOLDERS

During 2005, Yangarra continued to pursue its goal of developing core areas with high working interests and operatorship of those properties. In November 2005, Yangarra Resources Inc. merged with TriOil Ltd., which gave the company 100% working interest in the area of Medicine Hat and a new core area called Jaslan, located 140 km northeast of Edmonton. The merger also provided Yangarra with additional technical staff to support our exploration strategy.

A complete review of our non-core properties resulted in the sale of the Chinook, Paradise Valley and Marten Hills properties in 2005. In addition, Bayhurst Saskatchewan, and other area plays in Alberta – Mundare, Viking, Provost, Brazeau, and Bigstone – were put up for sale in April 2006. The proceeds from these properties will be used for debt reduction and development of our core areas.

Yangarra has assembled 140 sections of land with a 100% company owned compression facility in Medicine Hat. With 2 ½ years of production out of the first group of shallow gas wells, management is confident that exploration risk has been removed from the play. Drilling plans for 2006 are dependent on gas prices. In Ferrier, Yangarra owns 24 sections (averaging 40% working interest) and is in the process of drilling to earn another 12 sections (31.375% working interest). Yangarra also owns 50% of its 10 Mmcf/d compressor station and has extensive 3-D seismic coverage in the area. Four wells are planned for Ferrier in the remainder of 2006. In Jaslan, Yangarra owns eight sections (37.5% working interest) and an additional 5 sections (100% working interest). There is currently 200 boe/d of gas (6:1) behind pipe with production planned for mid summer 2006. An additional three wells are planned to be drilled in 2006.

Exploration plays to be explored in 2006 for the Company are in Corbett Creek (south of Grande Prairie, Alberta) and Mega (north of Manning, Alberta). In Corbett Creek a 50% interest has been farmed out in a Banff test with the farmee paying 80% of the drill and complete costs to earn 50% of the well, and four sections of land. In Mega, plans are underway by Yangarra to find a farmin partner to drill and complete a follow-up well to our 8-35-99-05W6 discovery drilled in January 2006.

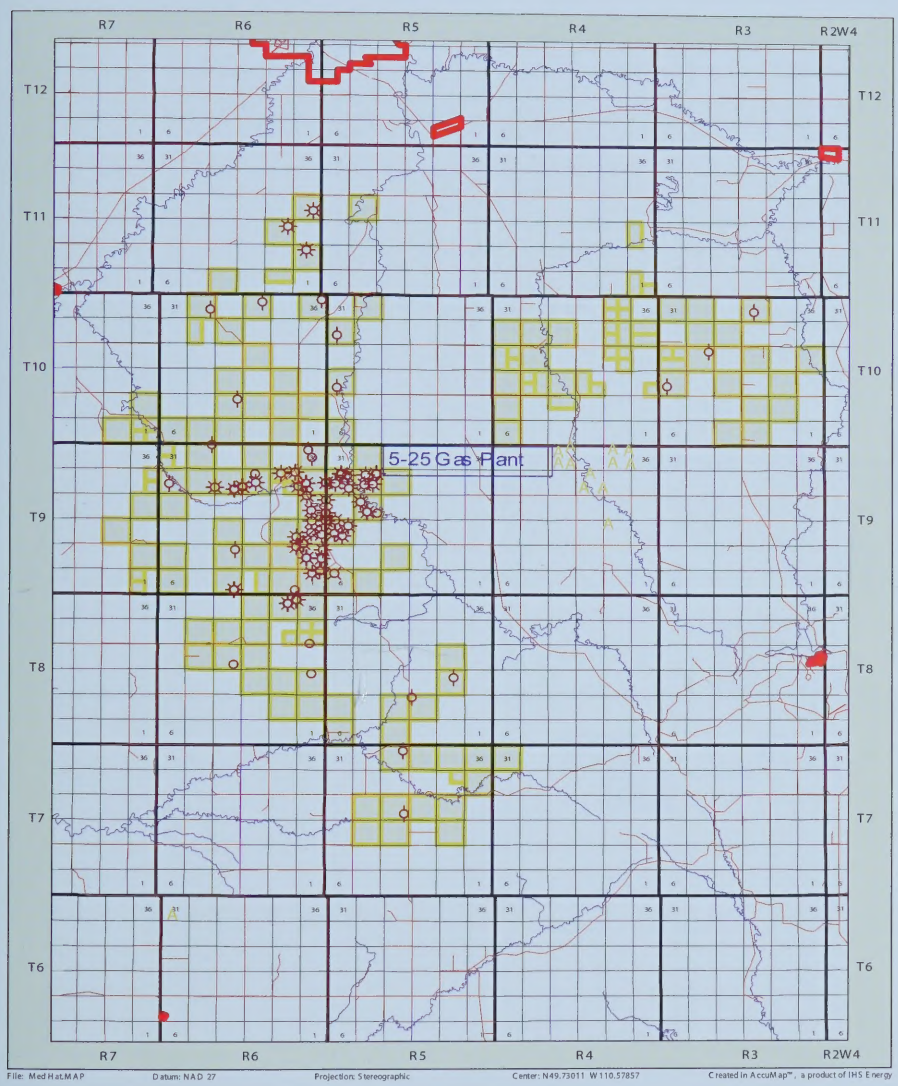
While gas prices have declined significantly since the end of 2005, there is ample upside in exploration in the Western Canadian sedimentary basin, and gas prices will ultimately strengthen. In the meantime, Yangarra's management will strive to keep the financial balance sheet in order and continue to refine our drill targets. In conclusion, Yangarra is committed to developing extensive land holdings and drill development wells in core areas.

We would like to thank our shareholders for their continued support in 2005 and look forward to a successful 2006.

Jim Evaskevich
President & CEO

OPERATIONS

MEDICINE HAT - ALBERTA

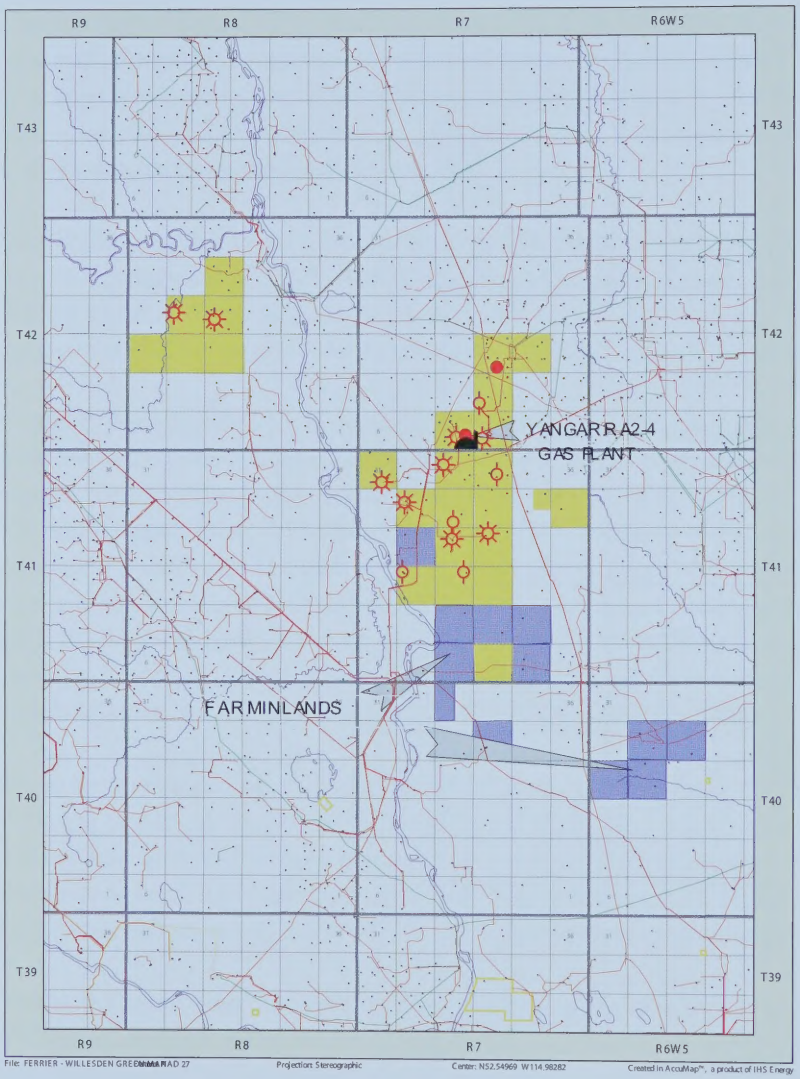


Medicine Hat

- 140 sections of land in this core area
- Compressor station situated at 5-25-9-6W4, built by Yangarra at the end of 2003
- Compressor station is capable of 4.0 mmcf/d and expandable to 8.0 mmcf/d
- 59 wells have been drilled on the property to date
- 37 tied in and on production
- Deeper Bow Island, Sawtooth and Sunburst potential
- 4 deep wells drilled
- Shallow Second White Specs / Medicine Hat zone wells
- 40 locations identified
- 4 wells per section on the shallow zones
- No exploration risk on the shallow horizons

OPERATIONS (cont'd)

FERRIER - ALBERTA

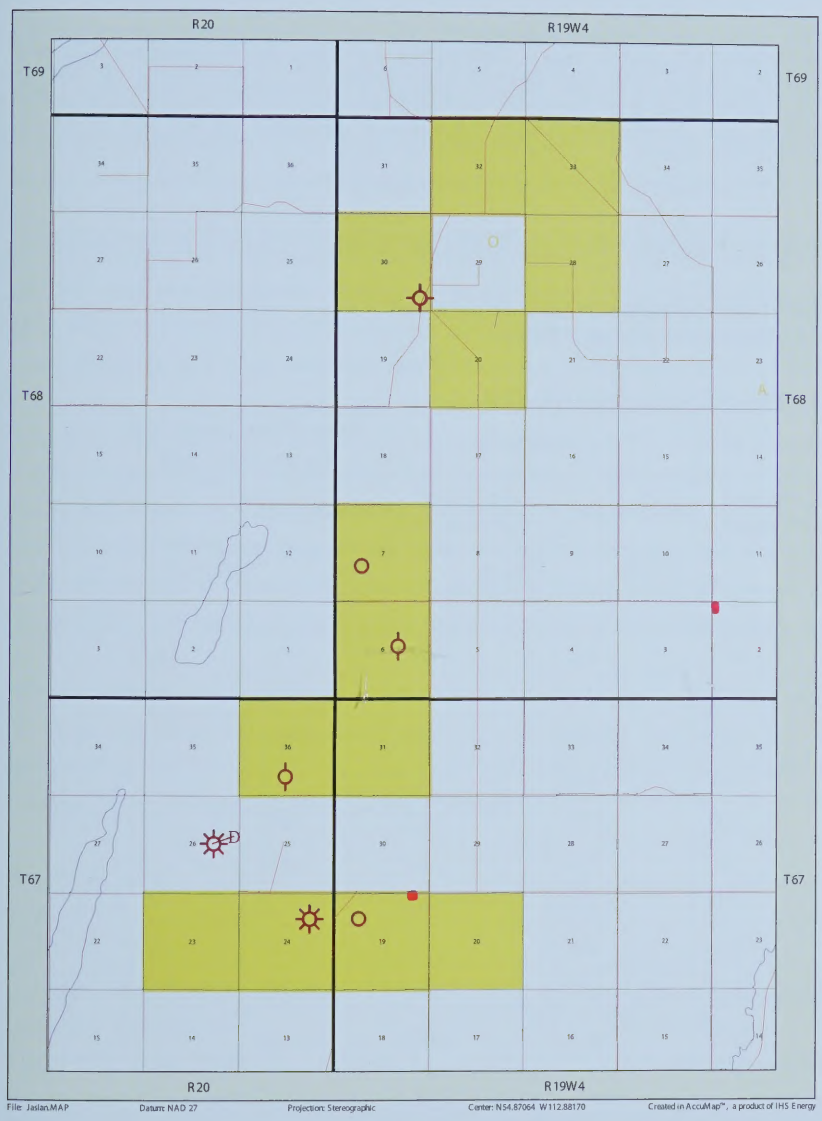


Ferrier

- 24 sections of land in this core area (average 40 % working interest)
- 12 section farm-in (31.375% working interest) – drill 2 wells to earn
- 10 Mmcf/d Compressor station - 50% working interest
- 3D Seismic data coverage over most of the property
- 17 wells drilled to date
- 12 wells currently producing
- Rock Creek/Ostracod and Viking production
- 2 wells to tie in
- Shallow Edmonton Sands, Notikewan, and Belly River potential
- 4 wells planned for 2006

OPERATIONS (cont'd)

JASLAN - ALBERTA



Jaslan

- 8 sections of land (average 37.5 % working interest)
- 5 section – 100% working interest
- 5 wells drilled to date
- Compressor station planned for summer 2006
- 200 boe/d gas behind pipe
- 3 wells planned for 2006

RESERVES

Corporate Reserves

The Company's reserves effective December 31, 2005 were evaluated by Sproule Associates Limited ("Sproule") in accordance with National Instrument 51-101. The Company's Statement of Reserves Data and Other Oil and Gas Information for the year ended December 31, 2005 is available on SEDAR at www.sedar.com.

The following table summarizes the Company's net shares of reserves using escalated pricing evaluations.

RECONCILIATION OF COMPANY NET RESERVES BY PRINCIPAL PRODUCT TYPE

ESCALATED PRICES AND COSTS

Factors	Light and Medium Oil		NGLS		Non-Associated and Associated Gas	
	Net Proved	Net Proved Plus Probable	Net Proved	Net Proved Plus Probable	Net Proved	Net Proved Plus Probable
	(Mbbl)	(Mbbl)	(Mbbl)	(Mbbl)	(MMcf)	(MMcf)
December 31, 2004						
Remaining Reserves	28.1	91.9	78.3	145.4	5,941	10,010
Production	-21.4	-21.4	-11.7	-11.7	-1,019	-1,019
Acquisitions	0.0	0.0	0.0	0.0	3,260	5,227
Dispositions	0.0	0.0	0.0	0.0	0	0
Discoveries	1.5	2.0	5.40	7.6	895	1,119
Extensions	0.0	0.0	0.0	0.0	272	313
Improved Recovery	0.0	0.0	0.0	0.0	0	0
Technical Revisions	20.5	-23.1	8.8	-7.2	-1,734	-3,097
Economic Factors	7.7	12.4	7.7	8.3	773	831
December 31, 2005 **Remaining Reserves**	36.4	61.9	88.5	142.4	8,388	13,384

Management's Responsibility

To the Shareholders of Yangarra Resources Ltd.

Management is responsible for the preparation and presentation of the accompanying financial statements, including responsibility for significant accounting judgments and estimates in accordance with Canadian generally accepted accounting principles and ensuring that all information in the annual report is consistent with the statements. This responsibility includes selecting appropriate accounting principles and methods, and making decisions affecting the measurement of transactions in which objective judgment is required.

In discharging its responsibilities for the integrity and fairness of the financial statements, management designs and maintains the necessary accounting systems and related internal controls to provide reasonable assurance that transactions are authorized, assets are safeguarded and financial records are properly maintained to provide reliable information for the preparation of financial statements.

The Board of Directors exercises its responsibilities for financial controls through an Audit Committee. The Audit Committee is responsible for overseeing management in the performance of its financial reporting responsibilities, and for approving the financial information included in the annual report. The Committee has the responsibility of meeting with management and external auditors to discuss the internal controls over the financial reporting process, auditing matters and financial reporting issues. The Committee is also responsible for recommending the appointment of the Company's external auditors.

Meyers Norris Penny LLP, an independent firm of Chartered Accountants, is appointed by the shareholders to audit the financial statements and report directly to them; their report follows. The external auditors have full and free access to, and meet periodically and separately with, both the Audit Committee and management to discuss their audit findings.

April 10, 2006

"James G. Evaskevich" (signed)
James G. Evaskevich
Chief Executive Officer

"Penny Payne" (signed)
Penny Payne
Chief Financial Officer

Auditors' Report

To the Shareholders of Yangarra Resources Ltd.:

We have audited the consolidated balance sheets of Yangarra Resources Ltd. as at December 31, 2005 and 2004, and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Calgary, Alberta

March 31, 2006

Meyers Norris Penny LLP

Chartered Accountants

Yangarra Resources Ltd.

Consolidated Balance Sheet

As at December 31

		2005		2004
Assets				
Current				
Cash	$	**81,671**	$	–
Accounts receivable		**2,667,511**		2,285,964
Prepaid expenses and deposits		**143,290**		170,015
		2,892,472		2,455,979
Goodwill *(note 4)*		**396,208**		–
Investment *(note 5)*		**109,258**		109,258
Property and equipment *(note 6)*		**42,150,409**		21,910,591
	$	**45,548,347**	$	24,475,828
Liabilities				
Current				
Bank indebtedness	$	**–**	$	178,565
Bank debt *(note 7)*		**9,450,000**		4,418,750
Accounts payable and accrued liabilities		**5,625,090**		3,775,316
		15,075,090		8,372,631
Asset retirement obligation *(note 8)*		**1,238,226**		394,648
Future income tax liability *(note 12)*		**4,090,121**		2,358,904
		20,403,437		11,126,183
Shareholders' Equity				
Share capital *(note 9)*		**31,188,344**		18,665,195
Contributed surplus *(note 10)*		**1,099,935**		730,307
Deficit		**(7,143,369)**		(6,045,857)
		25,144,910		13,349,645
	$	**45,548,347**	$	24,475,828

Approved on behalf of the Board of Directors

"James G. Evaskevich" (signed)

James G. Evaskevich

"Gordon A. Bowerman" (signed)

Gordon A. Bowerman

The accompanying notes are an integral part of these financial statements

Yangarra Resources Ltd.

Consolidated Statements of Operations and Deficit

For the years ended December 31

		2005		2004
Revenue				
Petroleum and natural gas sales	$	**8,354,853**	$	3,075,560
Royalties, net of Alberta Royalty Tax Credit		**(1,391,569)**		(620,852)
		6,963,284		2,454,708
Other income		**26,791**		–
		6,990,075		2,454,708
Expenses				
Production		**1,309,872**		560,742
Transportation costs		**120,043**		76,325
General and administrative		**1,152,511**		854,080
Interest		**397,309**		130,037
Stock-based compensation		**369,628**		199,691
Depletion and depreciation		**4,144,373**		1,854,858
Accretion		**34,154**		14,525
Impairment loss on investment		**–**		67,547
Write-down of mineral property		**–**		108,755
		7,527,890		3,866,560
Loss before income taxes		**(537,815)**		(1,411,852)
Income taxes				
Future income tax recovery *(note 12)*		**(271,468)**		(620,235)
Net loss for the year		**(266,347)**		(791,617)
Related party adjustment *(note 3)*		**(831,165)**		–
Deficit, beginning of year		**(6,045,857)**		(5,254,240)
Deficit, end of year	$	**(7,143,369)**	$	(6,045,857)
Loss per share – basic	$	**(0.01)**	$	(0.04)
Weighted average number of shares – basic		**31,228,861**		21,422,700

(1) Diluted loss per share has not been disclosed as the effect of options and warrants is anti-dilutive.

The accompanying notes are an integral part of these financial statements

Yangarra Resources Ltd.

Consolidated Statements of Cash Flows

For the yeras ended December 31

	2005	2004
Operating		
Net loss for the year	$ **(266,347)**	$ (791,617)
Add back non-cash items		
Other income	**(1,995)**	–
Stock-based compensation	**369,628**	199,691
Depletion and depreciation	**4,144,373**	1,854,858
Accretion	**34,154**	14,525
Write-down of mineral property	**–**	108,755
Impairment loss on investment	**–**	67,547
Future income tax provision	**(271,468)**	(620,235)
	4,008,345	833,524
Change in non-cash working capital *(note 13)*	**(280,299)**	2,601,589
	3,728,046	3,435,113
Financing		
Issue of equity instruments	**905,250**	8,813,368
Equity instrument issue costs	**(20,639)**	(688,320)
Proceeds from bank debt, net	**4,581,250**	4,418,750
Proceeds on repayment of related party advance *(note 3)*	**508,029**	–
	5,973,890	12,543,798
Investing		
Expenditures on and purchase of property and equipment	**(10,573,951)**	(14,368,824)
Proceeds on disposition of property and equipment	**300,000**	–
Proceeds on sale of marketable securities	**–**	252,727
Bank indebtedness acquired *(note 3)*	**(305,169)**	–
Amalgamation costs *(note 3)*	**(307,532)**	–
Changes in non-cash working capital *(note 13)*	**1,444,952**	(4,828,579)
	(9,441,700)	(18,944,676)
Increase (decrease) in cash during the year	**260,236**	(2,965,765)
(Bank indebtedness) cash, beginning of year	**(178,565)**	2,787,200
Cash (bank indebtedness), end of year	$ **81,671**	$ (178,565)
Supplemental cash flow information		
Interest paid	$ **319,091**	$ 130,170

The accompanying notes are an integral part of these financial statements

Yangarra Resources Ltd.

Notes to the Consolidated Financial Statements

For the years ended December 31, 2005 and 2004

1. Nature of operations and basis of presentation

Yangarra Resources Ltd. (the "Company") was formed by the amalgamation on November 9, 2005 (note 3), under the Business Corporations Act (Alberta) (the "ABCA"), of Yangarra Resources Inc. ("Predecessor Yangarra") and TriOil Ltd. ("TriOil"). The Company is involved in the production, exploration and development of resource properties.

Predecessor Yangarra was incorporated under the ABCA on January 22, 1985, as Ayrex Resources Ltd. The Company subsequently changed its name and began trading on the TSX Venture Exchange on July 21, 2003. TriOil was formed by the August 13, 2004 amalgamation of Entrada Energy Inc., a private company incorporated under the ABCA on November 16, 2000, and TriOil Ltd., a public company listed on the TSX Venture Exchange and incorporated under the ABCA on July 30, 2002.

In conjunction with the amalgamation, Predecessor Yangarra effected a 0.95 to 1 consolidation of its equity instruments. All equity instrument figures included herein are reflected on a post-consolidation basis.

These consolidated financial statements have been prepared on a going concern basis which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. As at December 31, 2005, the Company had a working capital deficit of $12,182,618 (2004 – $5,916,652) and an accumulated deficit of $7,143,369 (2004 – $6,045,857). Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due. The Company's ability to continue as a going concern is dependent upon its ability to attain profitable operations and generate funds therefrom and to continue to obtain capital financing from investors sufficient to meet current and future obligations.

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Yangarra Resources Corp.

2. Significant accounting policies

The consolidated financial statements have been prepared by management in accordance with generally accepted accounting principles in Canada. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts recorded in the financial statements and accompanying notes. Actual results could differ from these estimates. The consolidated financial statements have, in management's opinion, been properly prepared using careful judgment with reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

a) ***Cash and cash equivalents***

Cash and cash equivalents consist of bank balances (overdrafts) and term deposits with maturities of three months or less.

2. Significant accounting policies (continued)

b) Investments

Investments are stated at cost less provisions for other than temporary impairment, if any. Investments are classified as a long-term asset in concurrence with the nature of the investment.

c) Goodwill

Goodwill represents the excess of the cost of an acquisition over the net of the amounts assigned to assets acquired and liabilities assumed. Goodwill is not amortized but is tested for impairment at least annually.

The Company monitors its goodwill balance to determine whether any impairment has occurred. In order to make that determination, the Company bases the recoverability using the current and estimated cash flows of the underlying business on an undiscounted basis. If this review indicates that goodwill will not be recovered, the Company recognizes a write-down of the unamortized portion of goodwill in excess of its recoverable amount.

d) Property and equipment

The Company follows the full cost method of accounting for its petroleum and natural gas operations. Under this method all costs related to the acquisition of, exploration for, and development of petroleum and natural gas reserves are capitalized. Costs include lease acquisition costs, geological and geophysical expenses and costs of drilling both productive and non-productive wells and overhead costs directly related to exploration and development activities which have been charged in accordance with standard industry operating agreements. Proceeds from the sale of resource properties are applied against capitalized costs, without any gain or loss being realized, unless such sale would significantly alter the rate of depletion.

Depletion of resource properties and related equipment, net of estimated salvage or residual value, is provided using the unit of production method based upon estimated proven resource reserves before royalties, as determined by independent engineers. For depletion purposes, relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.

Other property and equipment, such as computer and office equipment and leasehold improvements ("office equipment"), are initially recorded at cost.

Depreciation is provided using methods and rates intended to depreciate the cost of office equipment over estimated useful lives.

2. Significant accounting policies (continued)

	Method	Rate
Computer equipment	declining balance	30 %
Leasehold improvements	straight-line	3 years
Office equipment	declining balance	20 %

In the year of acquisition, amortization is taken at one-half of the above rates.

e) *Long-lived assets*

Long-lived assets consist of property and equipment and resource properties. Long-lived assets held for use are measured, depleted or depreciated as described in the applicable accounting policies.

The Company performs impairment testing on long-lived assets held for use whenever events or changes in circumstances indicate that the carrying value of property and equipment or resource properties may not be recoverable. Impairment losses are recognized when undiscounted future cash flows from the Company's proved reserves, undeveloped land and future development projects are less than the carrying value of property and equipment and resource properties. Any impairment is included in earnings for the year.

If the carrying value is assessed not to be recoverable, an impairment loss is recognized to the extent that the carrying amount of the property and equipment and resource properties exceeds the sum of the discounted cash flows from proved plus probable reserves, undeveloped land and future development projects. The cash flows are estimated using expected future product prices and costs and are discounted using a risk-free interest rate.

f) *Investments in joint ventures*

Substantially all of the Company's petroleum and natural gas exploration and production activities are conducted jointly with others, and, accordingly, these financial statements reflect only the Company's proportionate interest in such activities.

g) *Bank debt*

The Company classifies borrowings as a current liability where the lender has a right to demand payment within twelve months, or where the lender may not re-finance the borrowing for a further lending period longer than twelve months.

h) *Asset retirement obligation*

Asset retirement costs and liabilities associated with site restoration and abandonment of long-lived assets

are initially measured at a fair value which approximates the cost a third party would incur in performing the tasks necessary to retire such assets. Such costs are capitalized as part of the cost of property and equipment and amortized to expense through depletion over the life of the asset. The change in the liability due to the passage of time is measured by applying an interest method of allocation to the opening liability and is recognized as an increase in the carrying value of the liability and an expense. The expense is recorded as accretion expense in the statement of operations. A change in the liability resulting from revisions to either the timing or the amount of the original estimate of undiscounted cash flows is recognized as an increase or decrease in the carrying amount of the liability, with an offsetting increase or decrease in the carrying amount of the associated asset.

i) Future income taxes

The Company follows the asset and liability method of accounting for future income taxes. Under this method, future income tax assets and liabilities are recorded based on temporary differences between the carrying amount of balance sheet items and their corresponding tax bases. In addition, the future benefits of income tax assets, including unused tax losses, are recognized, subject to a valuation allowance, to the extent that it is more likely than not that such future benefits will ultimately be realized. Future income tax assets and liabilities are measured using enacted tax rates and laws expected to apply when the tax liabilities or assets are to be either settled or realized.

j) Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Accounts receivable are stated after evaluation as to their collectibility and an appropriate allowance for doubtful accounts is provided where considered necessary. Amounts recorded for depletion of resource properties, amortization of property and equipment, asset retirement obligations and impairment calculations are based on estimates of natural gas and crude oil reserves and future costs required to develop those reserves. By their nature, these estimates of reserves, including the estimates of future prices and costs, and the related future cash flows are subject to measurement uncertainty, and the impact in the consolidated financial statements of future periods could be material. These assumptions are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

k) Flow through shares

Expenditure deductions for income tax purposes related to exploratory activities funded by flow-through equity instruments are renounced to investors in accordance with income tax legislation. The Company provides for the future effect on income taxes related to flow-through equity instruments as a reduction of share capital and an increase in future income tax liabilities when the renouncement documents are filed with taxation authorities.

2. Significant accounting policies (continued)

l) Stock-based compensation

Stock-based compensation expense is based on the estimated fair value of options granted at the time of the grant. The fair value is recognized in current earnings as stock-based compensation expense with a corresponding increase to contributed surplus over the vesting period of the options. Upon the exercise of the stock options, consideration paid together with the amount previously recognized in contributed surplus is recorded as an increase in share capital. In the event that vested options expire, previously recognized compensation expense associated with such stock options is not reversed. In the event that unvested options are cancelled, previously recognized compensation expense associated with such stock options is reversed.

m) Per share amounts

Basic earnings per share is calculated using the weighted average number of shares outstanding during the year. Diluted earnings per share is calculated based on the treasury stock method which assumes that any proceeds obtained on the exercise of options and warrants would be used to purchase common shares at the average price during the period. Diluted earnings per share is not disclosed where the effect of options and warrants is anti-dilutive.

n) Revenue recognition

Revenue is recognized from oil sales when the oil is delivered to the buyer and from gas sales when the gas passes through the pipeline at the delivery point.

o) Commodity contracts

Commodity contracts that do not meet the criteria for the use of hedge accounting are recorded on the balance sheet at fair value and changes in fair value are recognized in income in the period in which the change occurs.

3. Business acquisition and amalgamation

On November 9, 2005, Predecessor Yangarra and TriOil, companies related through common directors, completed a non-arm's length amalgamation. Pursuant to the amalgamation, the Company issued 0.95 shares for each outstanding share of Predecessor Yangarra, 0.95 options for each outstanding option of Predecessor Yangarra, one share for each outstanding TriOil share, one warrant for each outstanding TriOil warrant, and one option for each outstanding TriOil option. The transaction was accounted for as a purchase with Predecessor Yangarra deemed the acquirer.

As the amalgamation is a related party transaction, it has been measured at the carrying amount of the net

3. Business acquisition and amalgamation (continued)

assets acquired, as recorded in the accounts of TriOil. The difference between the carrying amount of the net assets and TriOil's share capital in the amount of $645,323 plus $185,842 of amalgamation costs incurred by Predecessor Yangarra (net of tax of $121,690), has been recorded as a charge to the Company's deficit.

The carrying amount has been allocated to TriOil's net assets as follows:

Current assets	$	1,449,621
Due to related party		508,029
Property and equipment		13,929,922
Goodwill		396,208
Bank indebtedness		(305,169)
Other current liabilities		(2,229,920)
Asset retirement obligation		(631,101)
Future income tax liability		(2,009,624)
Related party transaction adjustment, net of tax of $121,690		831,165
Net assets acquired	$	11,939,131
Purchase price		
24,219,700 common shares	$	11,631,599
Amalgamation costs		307,532
	$	11,939,131

4. Goodwill

Goodwill was acquired through the amalgamation between Yangarra and TriOil as described in note 3. Goodwill represents the excess of the cost over the net of the amounts assigned to assets acquired and liabilities assumed through the August 13, 2004 amalgamation between TriOil and Entrada Energy Inc. (see note 1).

5. Investment

As at December 31, 2005, the fair value of the Company's investment was estimated to be $75,800 (2004 – $109,258). The decline in value is not considered to be permanent.

6. Property and equipment

	December 31, 2005		
	Cost	Accumulated depletion and depreciation	Net book value
Office equipment	$ 237,094	$ 57,973	$ 179,121
Petroleum and natural gas properties	48,649,879	6,678,591	41,971,288
	$ 48,886,973	$ 6,736,564	$ 42,150,409

	December 31, 2004		
	Cost	Accumulated depletion and depreciation	Net book value
Office equipment	$ 77,007	$ 20,210	$ 56,797
Petroleum and natural gas properties	24,425,776	2,571,981	21,853,794
	$ 24,502,782	$ 2,592,191	$ 21,910,591

During the year, property and equipment additions totaled $24,684,191 (2004 - $14,541,445) of which $180,318 (2004 - $172,621) was due to asset retirement obligations and $13,929,922 (2004 - $ nil) was acquired through the business acquisition and amalgamation described in note 3.

At December 31, 2005, the Company has excluded $1,266,105 (2004 - $3,214,845) of resource properties relating to unproved properties from the depletion calculation and impairment test. Unproved properties have been separately evaluated by management for impairment. In addition, $9,263,750 (2004 - $7,467,000) of future development costs were included in the depletion calculation.

The Company did not capitalize any general and administrative costs during 2005 or 2004 other than to the extent of the Company's working interest in operated capital expenditure programs on which operator's fees have been charged in accordance with standard industry operating agreements.

6. Property and equipment (continued)

The Company applied the ceiling test to its capitalized assets as at December 31, 2005 and determined that there was no impairment. For purposes of this impairment test, the following future commodity prices were used:

	Edmonton Par Price Cdn $/bbl	Alberta AECO-C Spot Cdn $/mcf
2006	70.07	11.58
2007	70.99	10.84
2008	62.73	8.95
2009	57.53	7.87
2010	54.65	7.57
Escalation rate thereafter	1.5%	1.5%

7. Bank debt

	2005	*2004*
Revolving operating demand loan available to a maximum of $11,500,000 (2004 - $5,500,000), requiring payments of interest only subject to availability, lender's review and right of demand. Interest is calculated daily and payable monthly at prime plus 0.5% (2004 – prime plus 0.75%).	$ 9,450,000	$ 3,575,000
Demand loan available to a maximum of $1,000,000 bearing interest at prime plus 1% and repayable in monthly principal payments of $31,250 over the half-life of proved petroleum and natural gas reserves.	–	843,750
	$ 9,450,000	$ 4,418,750

In November 2005, the Company revised the credit facilities with its lender, following the amalgamation described in note 3. In addition to the revolving operating demand loan facility, the Company has a treasury risk line available for interest rate, foreign exchange and commodity risk management. The treasury risk line is repayable per contract maturities. As at December 31, 2005 and 2004, there were no amounts outstanding under the treasury risk line.

The credit facilities are secured by a general assignment of book debts, a $10,000,000 debenture, a $35,000,000 supplemental debenture, evidence of insurance coverage with the lender as first loss payee, title representation of petroleum and natural gas reserves, and assignment of revenues and monies under material contracts. The debentures contain a floating charge over all assets of the Company with a negative pledge and undertaking to provide fixed charges on the Company's major producing petroleum and natural gas reserves.

7. Bank debt (continued)

Pursuant to the terms of the credit facilities, the Company is subject to a financial covenant with respect to working capital. As at December 31, 2005, the Company was in breach of the covenant and has obtained a letter from the lender acknowledging the breach. The revolving operating demand loan is a current liability by its nature therefore no reclassification between long-term and current liabilities is required.

8. Asset retirement obligation

The following table presents the reconciliation of the carrying amount of the obligation associated with the retirement of the Company's property and equipment:

		a) 2005		*2004*
Asset retirement obligation, beginning of year	$	394,648	$	207,502
Liabilities acquired *(note 3)*		631,101		–
Liabilities incurred		159,167		172,621
Dispositions		(10,861)		–
Effect of change in estimates		30,017		–
Accretion		34,154		14,525
Asset retirement obligation, end of year	$	1,238,226	$	394,648

The following significant assumptions were used to estimate the asset retirement obligation:

		2005		*2004*
Undiscounted cash flows	$	2,343,048	$	1,425,122
Discount rate		7%		7%
Inflation rate		2%		2%
Weighted average expected timing of cash flows		9.5 years		17.5 years

9. Share capital

All share capital figures included herein are on a post-consolidation basis (see notes 1 and 3).

a) Authorized

Unlimited number of common shares, without nominal or par value
Unlimited number of first preferred shares, without nominal or par value
Unlimited number of second preferred shares, without nominal or par value

9. Share capital (continued)

b) Issued

Common shares	Number of shares		Amount
a) Balance, December 31, 2003	**17,304,725**	$	**11,934,349**
Private placement of common shares (i)	2,375,000		3,625,000
Private placement of flow-through shares (ii)	6,089,741		4,999,998
Exercise of warrants (iii)	268,375		84,750
Exercise of options (iv)	307,325		159,004
Tax effect of flow-through shares	–		(1,680,999)
Share issue costs, net of tax of $231,413	–		(456,907)
Balance, December 31, 2004	**26,345,166**	$	**18,665,195**
Exercise of warrants (v)	2,866,625		905,250
Issued in relation to amalgamation *(note 3)*	24,219,700		11,631,599
Share issue costs, net of tax of $6,939	–		(13,700)
Balance, December 31, 2005	**53,431,491**	$	**31,188,344**

i) On April 7, 2004, the Company completed a financing of 2,375,000 common shares at a price of $1.53 per common share for gross proceeds of $3,625,000.

ii) On November 8, 2004, the Company completed a financing of 6,089,741 common shares on a "flow-through" basis at a price of $0.82 per share for gross proceeds of $4,999,998. These proceeds were renounced to investors on December 31, 2004 and the Company had until December 31, 2005 to incur qualifying expenditures. As at December 31, 2005, all expenditures had been incurred.

iii) During 2004, 268,375 shares were issued on the exercise of the same number of warrants at an exercise price of $0.32 per share for gross cash proceeds of $84,750.

iv) During 2004, 307,325 shares were issued on the exercise of the same number of options at a weighted average exercise price of $0.34 per share for total cash proceeds of $103,620 plus a pro-rata share of the related fair value previously recorded to contributed surplus in the amount of $55,384.

v) During 2005, 2,866,625 shares were issued on the exercise of the same number of warrants at an exercise price of $0.32 per share for gross cash proceeds of $905,250.

9. Share capital (continued)

c) *Stock options*

The Company has a stock option plan under which the Board of Directors may grant options to directors, officers, other employees and key consultants. The purpose of the plan is to advance the interests of the Company by encouraging these individuals to acquire shares in the Company and thereby remain associated with, and seek to maximize the value of, the Company. Under the plan, the number of shares reserved for issuance pursuant to the exercise of all options under the plan may not exceed 10% of the issued and outstanding common shares on a non-diluted basis at any time. The options expire not more than five years from the date of grant, or earlier if the individual ceases to be associated with the Company, and vest over terms determined at the time of grant.

During 2005, the Company granted the following options with an expiry of five years from the date of grant:

Date of grant	Number of options	Exercise price	Vesting term	Total estimated fair value	Related 2005 portion of stock-based compensation expense (note 10)
February 2005	665,000	$0.74	Immediately	$ 290,850	$ 290,850
September 2005	123,500	0.45	Immediately	39,347	39,347
September 2005	142,500	0.45	Two years	43,294	9,519
November 2005	999,175	0.50	Two years	348,100	22,173
	1,930,175				$ 361,889

The Black-Scholes option pricing model was used to estimate the fair value of options granted based on the following significant assumptions:

	2005	*2004*
Risk-free interest rate	3.5% to 5%	3.75%
Expected volatility	75% to 86%	50%
Expected life	5 years	5 years

Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Company's stock options. For the purposes of recording stock-based compensation, the estimated fair value of the options is recognized over the vesting period of the option.

9. Share capital (continued)

c) *Stock options (continued)*

The following tables summarize information about stock options outstanding as at:

	December 31, 2005		December 31, 2004	
	Options	Weighted – Average Exercise Price	Options	Weighted – Average Exercise Price
Opening	1,946,550	$ 0.76	1,645,875	$ 0.57
Granted	1,930,175	0.58	1,173,250	1.19
Acquired (note 3)	2,045,000	0.55	–	–
Exercised	–	–	(307,325)	0.34
Cancelled	(671,625)	0.68	(565,250)	1.59
Closing	5,250,100	$ 0.62	1,946,550	$ 0.76

	December 31, 2005			
Range of Exercise Price	Number Outstanding	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price	Number Exercisable
$ 0.21 – $ 0.45	542,450	3.66	$ 0.39	406,450
$ 0.46 – $ 0.55	2,500,175	4.33	0.52	800,667
$ 0.63 – $ 0.74	900,750	3.66	0.69	811,083
$ 0.79 – $ 1.05	1,306,725	3.30	0.87	1,306,725
	5,250,100	3.89	$ 0.62	3,324,925

9. Share capital (continued)

c) Stock options (continued)

d) Warrants

The following table summarizes information about warrants outstanding as at:

	December 31, 2005		December 31, 2004	
	Warrants	Weighted – Average Exercise Price	Warrants	Weighted – Average Exercise Price
Opening	2,866,625	$ 0.29	3,135,000	$ 0.29
Acquired (note 3)	1,328,711	0.87	–	–
Exercised	(2,866,625)	0.29	(268,375)	0.29
Expired	(137,049)	0.65	–	–
Closing	1,191,662	$ 0.90	2,866,625	$ 0.29

All 1,191,662 warrants outstanding at December 31, 2005 are exercisable and have a weighted average remaining contractual life of 0.17 years. These warrants expired unexercised in March 2006.

10. Contributed surplus

		2005	2004
Balance – beginning of year	$	730,307	586,000
Stock-based compensation – options granted in 2005 / 2004		361,889	199,691
Stock-based compensation – options acquired on amalgamation		14,911	–
Stock-based compensation on unvested cancelled options (note 9(c))		(7,172)	–
Stock-based compensation on exercised options (note 9(b)(iv))		–	(55,384)
Balance – end of year	$	1,099,935	730,307

11. Commodity contracts

During 2005, the Company entered into a Commodity European Producer Collar to sell 1000 GJ of gas per day to a third party from May 1, 2005 to December 31, 2005 at a ceiling price of $9 per GJ and a floor price of $7 per GJ. As at December 31, 2005, the Company had fulfilled the terms of the Collar.

During 2004, the Company entered Commodity Put Option to sell 2500 GJ of gas per day to a third party from May 1, 2004 to October 31, 2004 at a strike price of $5 per GJ and a total premium cost to the Company of $65,780 based on $0.143 per GJ. As at December 31, 2004, the Company had fulfilled the terms of the Option.

12. Income taxes

The provision for future income taxes differs from the amount computed by applying the combined federal and provincial tax rates to the loss before taxes. The difference results from the following:

		2005		2004
Expected income tax recovery at 37.62% (2004 – 38.87%)	$	(202,326)	$	(548,786)
Non-deductible crown and other charges		290,065		184,477
Stock-based compensation		139,054		77,620
Amalgamation costs		(76,793)		–
Resource allowance		(181,585)		(115,468)
Alberta Royalty Tax Credit		(93,224)		(59,033)
Attributed Canadian Royalty Income		(13,814)		(24,312)
Rate adjustments and other		(132,845)		(134,733)
	$	(271,468)	$	(620,235)

The components of future income taxes at December 31 are:

		2005		2004
Future income tax assets				
Asset retirement obligation	$	416,292	$	132,681
Non-capital loss carryforwards		389,026		221,714
Share issue costs		343,996		259,317
Amalgamation costs		121,690		–
Attributed Canadian Royalty Income		90,858		26,787
Other		–		22,709
Future income tax liabilities				
Carrying amount of property and equipment in excess of tax basis		(5,451,983)		(3,022,112)
	$	(4,090,121)	$	(2,358,904)

As at December 31, 2005, the Company has approximately $27 million of tax pools available for deduction against future taxable income. The Company also has non-capital tax losses of $1.2 million available for deduction against future taxable income that expire between 2006 and 2014.

13. Change in non-cash working capital

		2005		2004
Accounts receivable	$	1,024,736	$	(390,912)
Prepaid expenses and deposits		70,063		(111,003)
Accounts payable and accrued liabilities		69,854		(1,725,075)
	$	1,164,653	$	(2,226,990)

The change in non-cash working capital has been allocated to the following activities:

		2005		2004
Operating	$	(280,299)	$	2,601,589
Investing		1,444,952		(4,828,579)
	$	1,164,653	$	(2,226,990)

14. Commitments

a) The Company has entered into lease agreements for office premises and equipment with estimated minimum annual payments as follows:

2006	$ 363,597
2007	224,097
2008	73,708

b) In January 2006, the Company entered into a six month contract with an investor relations firm at a fee of $5,810 per month (US$5,000), plus expenses. The Company may renew the contract under the same terms for an additional six months with prior written notice.

15. Related party transactions

Except as disclosed elsewhere in these financial statements, the Company had the following related party transactions:

a) During the years ended December 31, 2005 and 2004, the Company was charged or invoiced the following amounts by certain of its officers and directors and by companies controlled by certain of the Company's officers and directors:

		2005		2004
Administration and consulting fees	$	284,454	$	169,911
Production and capital expenditures	$	293,070	$	2,798,403

15. Related party transactions (continued)

b) During the year ended December 31, 2005, the Company was charged $103,341 (2004 – $60,746) by a law firm in which a director of the Company is a partner.

Included in accounts payable and accrued liabilities is $147,007 (2004 - $167,720), and in accounts receivable is $nil (2004 – $1,225,319), relating to the above transactions. These transactions were in the normal course of operations and were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

16. Financial instruments

The Company, as part of its operations, carries a number of financial instruments. It is management's opinion that the Company is not exposed to significant interest or currency risks arising from these financial instruments except as otherwise disclosed.

a) Fair value

The carrying amount of cash, accounts receivable, bank indebtedness, bank debt and accounts payable and accrued liabilities approximates their fair value due to the short-term maturities of these items.

b) Credit risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of trade accounts receivable. The majority of the Company's accounts receivable are in respect of oil and natural gas operations with joint venture partners and are therefore subject to normal industry risks. Company sales are concentrated in the oil and gas industry.

c) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument might be adversely affected by a change in the interest rates. In seeking to minimize the risks from interest rate fluctuations, the Company manages exposure through its normal operating and financing activities. The Company is exposed to interest rate risk primarily through its variable interest rate bank loans.

d) Commodity price risk

The Company's operations are exposed to commodity price fluctuations. The Company was not a party to any hedging arrangements as at December 31, 2005 (see note 11) and up to the date of the audit report.

17. Subsequent event

In February 2006, the Company granted 150,000 options to two companies providing consulting and investor relations services. 75,000 options are exercisable at $0.71 per share and vest over two years and 75,000 options are exercisable at $0.70 per share and vest over five years. An additional 10,000 options were granted to an employee with a vesting period of two years and an exercise price of $0.66 per share. All of the options expire 5 years from the date of grant.

18. Comparative figures

Certain prior year comparative figures have been reclassified to conform to the presentation used in the current year.

Management's discussion and analysis ("MD&A") of the financial condition and the results of operations should be read in conjunction with the audited consolidated financial statements of Yangarra Resources Ltd. (the "Company") for the years ended December 31, 2005 and 2004, together with the accompanying notes. The MD&A has been prepared using information that is current to April 10, 2006.

The financial information presented herein has been prepared on the basis of Canadian generally accepted accounting principles ("GAAP"). Throughout this discussion, percentage changes are calculated using numbers rounded to the decimal to which they appear. All references to dollar amounts are in Canadian dollars.

***BOE Presentation** – Production information is commonly reported in units of barrel of oil equivalent ("boe"). For purposes of computing such units, natural gas is converted to equivalent barrels of oil using a conversion factor of six thousand cubic feet to one barrel of oil. This conversion ratio of 6:1 is based on an energy equivalent wellhead value for the individual products. Such disclosure of boe may be misleading, particularly if used in isolation. Readers should be aware that historical results are not necessarily indicative of future performance.*

***Special Note Regarding Non-GAAP Measures** – This MD&A includes references to financial measures commonly used in the oil and gas industry. The terms "net petroleum and natural gas revenue" (petroleum and natural gas sales less royalties, production expenses and transportation costs) and "funds flow from operations" (net loss for the period adjusted for non-cash items in the statement of operations) are not measures GAAP and do not have standardized meanings prescribed by GAAP.*

***Forward-looking Statements** – Certain information regarding the Company set forth in this report, including management's assessment of the Company's future plans and operations, contain forward-looking statements that involve substantial known and unknown risks and uncertainties. These risks and uncertainties, many of which are beyond the Company's control, include the impact of general economic conditions and specific industry conditions, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, the lack of available qualified personnel or management, stock market volatility and ability to access sufficient capital from internal and external sources. The Company's actual results, performance or achievements could differ materially from those expressed in, or implied by, these forward-looking statements, and accordingly, no assurance can be given that any events anticipated by the forward-looking statements will transpire or occur, or if any of them do, what benefits the Company can derive such events.*

Company History

On November 9, 2005, Yangarra Resources Inc. ("Yangarra") and TriOil Ltd. ("TriOil"), companies related through common directors, completed a non-arm's length amalgamation ("Amalgamation") to form Yangarra Resources Ltd. (the "Company", symbol "YAN"). Pursuant to the Amalgamation, the Company issued 0.95 shares for each outstanding share of Yangarra and 0.95 options each outstanding option of Yangarra, and one share for each outstanding TriOil share, one warrant for each outstanding TriOil warrant, and one option for each outstanding TriOil option. The transaction was accounted for as a purchase with Yangarra deemed the acquirer.

Yangarra Resources Ltd.

Management's Discussion and Analysis

For the years ended December 31, 2005 and 2004

As the Amalgamation was a related party transaction, it was measured at the carrying amount of the net assets acquired, as recorded in the accounts of TriOil. The difference between the carrying amount of the net assets and TriOil's share capital in the amount of $645,323 plus $185,842 of Amalgamation costs incurred by Yangarra (net of tax of $121,690) has been recorded as an adjustment to the Company's deficit.

Predecessor Yangarra was incorporated under the laws of the Province of Alberta on January 22, 1985, as Ayrex Resources Ltd ("Ayrex", symbol AYX). Ayrex subsequently changed its name to Yangarra Resources Inc. and began trading on the TSX Venture Exchange on July 21, 2003. TriOil was formed by the August 13, 2004 amalgamation of Entrada Energy Inc., a private company incorporated on November 16, 2000, and TriOil Ltd., a public company listed on the TSX Venture Exchange and incorporated on July 30, 2002.

Results of Operations

	Three months ended December 31		Year ended December 31	
	2005	2004	2005	2004
Statement of Operations and Deficit				
Petroleum and natural gas sales ($)	3,231,966	1,116,081	8,354,853	3,075,560
Petroleum and natural gas sales per boe ($)	64.89	41.65	55.59	39.75
Net Petroleum and natural gas revenue ($)	2,211,174	700,515	5,533,369	1,817,641
Net petroleum and natural gas revenue per boe ($)	44.40	26.14	36.81	23.49
Daily sales volumes (boe 6:1)	541	291	582	211
Income (loss) for the period ($)	134,136	(22,734)	(266,347)	(791,617)
Income (loss) per share – basic and diluted ($)	–	–	(0.01)	(0.04)
Statement of Cash Flows				
Funds flow from operations ($)	1,472,621	(610,235)	4,008,345	833,524
Weighted average number of shares – basic	42,901,182	24,915,864	31,228,861	21,422,700

As a result of the Amalgamation, the Company increased its working interest in the Medicine Hat area from 50% to 100% and acquired properties in the Inland/Mundare, Jaslan, Provost, Bigstone and Viking South areas of Alberta containing 14 producing wells, excluding Medicine Hat. During 2005, the Company continued exploration and development programs in the Medicine Hat, Mitsue, Grande Prairie, Mega, Ferrier, Inland/Mundare and Jaslan areas of Alberta and in Bayhurst, Saskatchewan. The 2005 drilling program consisted of two gas wells, two oil wells, one reentry and one abandoned well drilled in Ferrier; nine gas wells drilled and tied in at Medicine Hat with one additional well (40%WI) acquired by tieing the well into Company-owned facilities in that area; one oil well drilled and put on stream in Mitsue; a dry and abandoned well drilled at Grande Prairie; one gas well drilled at Jaslan; and one gas well drilled in Bayhurst Saskatchewan.

The three months and year ended December 31, 2005 results of operations are those of Yangarra and include TriOil from November 9 to December, 2005.

Fourth Quarter Results

Net petroleum and natural gas revenue for the three months ended December 31, 2005 was $2,221,174 ($44.40/boe) compared to $700,515 ($26.14/boe) for the 2004 comparative period. The increase is explained by changes in the following components:

- Petroleum and natural gas sales before royalties were $3,231,966 (541 boe/day) for the three months ended December 31, 2005 compared to $1,116,081 (291 boe/day) for the same 2004 quarter. The increase in sales is attributed to an increase in prices from $41.65/boe for the fourth quarter of 2004 to $64.89/boe for 2005 plus an increase in production primarily due to the Amalgamation.
- Royalties, net of the Alberta Royalty Tax Credit, in the fourth quarter of 2005 varied only slightly on both a boe basis and percentage basis from those for 2004. They were $512,813 ($7.59/boe or 16% of sales) for the three months ended December 31, 2005 as compared to $194,606 ($7.26/boe or 17% of sales) for the three months ended December 31, 2004.
- Production and transportation costs were $507,979 ($10.20/boe) for the three months ended December 31, 2005 compared to $220,960 ($8.25/boe) for the same 2004 quarter. The increase in 2005 is due to generally higher industry costs as well as higher costs in a few of the areas acquired through the Amalgamation, including annual lease rentals.

General and administrative expenses for the three months ended December 31, 2005 were $576,767 compared to $422,234 for the three months ended December 31, 2004. The overall increase in general and administrative expenses is commensurate with the increase in the size of the Company since the November Amalgamation, including an increase in leased office space and administrative needs.

Interest expense for the fourth quarter of 2005 was $186,582 compared to $54,992 for 2004. The increase in interest is due to 2005 Part XII.6 interest on unspent flow-through expenditure commitments resulting from flow-through shares issued in 2004 and an increase in the use of the revolving operating demand loan.

Stock-based compensation expense for the fourth quarter of 2005 was a net credit of $3,863 due to the compensation expense related to options granted in 2005 recorded over the options' vesting periods offset by the reversal of previously recorded stock-based compensation expense related to the unvested portion of options cancelled in the quarter. Stock-based compensation expense for the fourth quarter of 2004 was a credit of $297,309 due primarily to year end changes in the estimates used to fair value options granted in prior 2004 quarters.

Depletion and depreciation expense for the three months ended December 31, 2005 was $1,325,376 compared to $855,030 for the three months ended December 31, 2004. The increase is due to increases in the Company's asset base and production volumes, primarily related to the Amalgamation.

Accretion expense for the three months ended December 31, 2005 was a net credit of $18,942 compared

to an expense of $3,631 due to the reclassification of asset retirement obligation components related to liability additions that had been recorded as accretion expense in previous 2005 quarters.

Annual Results

Net petroleum and natural gas revenue for the year ended December 31, 2005 was $5,533,369 ($36.81/boe) compared to $1,817,641 ($23.49/boe) for 2004. The increase is explained by changes in the following components:

- Petroleum and natural gas sales before royalties were $8,354,853 (582 boe/day) for the year ended December 31, 2005 compared to $3,075,560 (211 boe/day) for 2004. The increase in sales is attributed to an increase in average prices from $39.75/boe earned in 2004 to $55.59/boe earned in 2005 plus an increase in production primarily due to the results of the Company's drilling program and to the Amalgamation. Production prior to the Amalgamation for the nine months ended September 30, 2005 averaged 368 boe/day compared to 185 boe/day for the same 2004 period.
- Royalties, net of the Alberta Royalty Tax Credit, for all of 2005 were $1,391,569 compared to $620,852 for 2004. As a percentage of sales, royalties decreased slightly from 20% in 2004 to 17% in 2005 due to capital cost adjustments for processing the Crown's portion of gas.
- Production and transportation costs were $1,429,915 ($9.51/boe) for the year ended December 31, 2005 compared to $637,067 ($8.23/boe) for the year ended December 31, 2004. The increase in 2005 is due to generally higher industry costs.

General and administrative expenses for 2005 were $1,152,511 compared to $854,080 for 2004. The increase in general and administrative expenses is commensurate with the overall increase in corporate and production activities plus the increase in the size of the Company since the November Amalgamation, including an increase in leased office space and administrative needs.

Interest expense for the year ended December 31, 2005 was $397,309 compared to $130,037 for 2004. The increase in interest is due to 2005 Part XII.6 interest on unspent flow-through expenditure commitments resulting from flow-through shares issued in 2004 and an increase in the use of the revolving operating demand loan.

Stock-based compensation expense increased from $199,691 in 2004 to $369,628 in 2005 due to an increase in the number of options granted coupled with changes in the assumptions used to estimate the fair value of options plus stock-based compensation related to options acquired through the Amalgamation.
Depletion and depreciation expense for 2005 was $4,144,373 compared to $1,854,858 for 2004. The increase is due to increases in the Company's asset base and production volumes, related to the Company's drilling program and the Amalgamation.

Accretion expense for 2005 was $34,154 compared to $14,525 due to the increase in the number of wells resulting from the Amalgamation and the Company's drilling program.

During the year ended December 31, 2005, the Company generated $4,008,345 of funds flow from operations compared to $833,524 generated in 2004. The improvement in funds flow was due primarily to the increase in net petroleum and natural gas revenues.

Liquidity and Capital Resources

During the three months and year ended December 31, 2005, the Company generated $1,472,621 and $4,008,345, respectively, of funds flow from operations compared to $223,289 and $833,524, respectively, generated in the 2004 comparative periods. The improvement in funds flow was due primarily to the increase in net petroleum and natural gas revenues.

As at December 31, 2005, the Company had a working capital deficit of $12.2 million compared to a deficit of $5.9 million at December 31, 2004. The increase in the working capital deficit was due to a $10.3 million net capital spending program for the year plus $0.3 of Amalgamation costs and $0.3 of bank indebtedness acquired from TriOil offset by the $4.0 million of funds flow generated by operating activities and $0.9 million of proceeds from the exercise of warrants. The capital spending program was financed by the $4.0 million funds flow from operations, $0.9 million of warrant proceeds, $4.6 million of proceeds from the revolving operating demand loan and the balance through accounts payable.

In November 2005, the Company revised the credit facilities with its lender, following the Amalgamation. In addition to the $11.5 million revolving operating demand loan facility, the Company has a treasury risk line available for interest rate, foreign exchange and commodity risk management. The treasury risk line is repayable per contract maturities. As at December 31, 2005 and 2004, there were no amounts outstanding under the treasury risk line. Pursuant to the terms of the credit facilities, the Company is subject to a financial covenant with respect to working capital. As at December 31, 2005, the Company was in breach of the covenant and has obtained a letter from the lender acknowledging the breach.

The Company did not engage in any financing activities during 2005. Proceeds from share issuances related to the exercise of warrants issued in 2003. The Company has no off-balance sheet arrangements. Financial instruments consist of those shown on the balance sheet.

Capital Spending

During the three months and year ended December 31, 2005, the Company spent $4,494,023 and $10,573,951 respectively, on its capital spending program compared to $5,290,353 and $14,368,824, respectively, for the three months and year ended December 31, 2004. 2005 capital spending is summarized as follows:

	December 31, 2005	
	Three months ended	Year ended
Land	$ 26,466	$ 331,271
Drilling and completion	2,756,338	6,740,860
Geological and geophysical	808,945	1,260,404
Equipment	890,852	2,162,855
Other	11,422	78,561
	$ 4,494,023	$ 10,573,951

The Company also added $13,929,922 of property and equipment in November 2005 as a result of the Amalgamation.

2005 drilling activity

	Three months ended December 31, 2005		Year ended December 31, 2005	
	Gross	Net	Gross	Net
Light and medium oil	1.0	0.33	3.0	1.20
Natural gas	7.0	3.81	15.0	8.02
Dry	1.0	0.60	2.0	0.92
	9.0	4.74	20.0	10.14

Flow-through expenditures

In November 2004, the Company issued a total of 6,089,741 common shares on a "flow-through" basis at a price of $0.82 per share for gross proceeds of $4,999,998. These proceeds were renounced to investors on December 31, 2004. Approximately $901,532 of related qualifying expenditures were incurred in 2004 and the balance of approximately $4,098,466 was incurred in 2005. In addition, the Company acquired a flow-through commitment of approximately $1,615,081 from TriOil as a result of the Amalgamation. The related qualifying expenditures were incurred in November and December 2005.

Asset retirement obligation

As at December 31, 2005, the undiscounted fair value of the asset retirement obligation associated with the Company's existing properties was estimated to be $2,343,048 for which $1,238,226 has been recorded using a discount rate of 7%, an inflation rate of 2% and an estimated weighted average timing of cash flows of 9.5 years.

Related Party Transactions

The Company's related party transactions consisted of:

a) The Amalgamation, as described under "Corporate History";
b) Amounts charged and/or invoiced by certain of its officers and directors and by companies controlled by certain of the Company's officers and directors:

		2005		2004
Administration and consulting fees	$	284,454	$	169,911
Production and capital expenditures	$	293,070	$	2,798,403

c) $103,341 (2004 – $60,746) of fees by a law firm in which a director of the Company is a partner.

Share Capital

In conjunction with the Amalgamation, the Yangarra effected a 0.95 to 1 share consolidation of its share capital. All share capital figures included herein are on a post-consolidation basis.

The Company commenced 2005 with a total of 26,345,166 shares with a book value of $18,665,195. During February, March and July 2005, 2,866,625 warrants were exercised for the same number of common shares for net proceeds of $905,250. In November 2005, the Company issued 24,219,700 shares in the Amalgamation. As at December 31, 2005, there were 53,431,491 issued and outstanding shares with a book value of $31,188,344. Subsequent to year end, 265,500 shares were issued on the exercise of stock options, resulting in 53,696,991 common shares outstanding as of the date of this MD&A.

At the beginning of 2005, there were 1,946,550 stock options outstanding. During the year a total of 1,930,175 options were granted, 2,045,000 options were assumed on the Amalgamation and 671,625 options were cancelled. The resulting number of options outstanding at December 31, 2005 was 5,250,100 of which 3,324,925 were exercisable. Subsequent to year end, an additional 160,000 options were granted, 265,500 options were exercised and 245,625 options were cancelled, resulting in 4,898,975 stock options outstanding as of the date of this MD&A.

At the beginning of 2005, there were 2,866,625 warrants outstanding, all of which were exercised during the

year. As a result of the Amalgamation, the Company assumed 1,328,711 warrants, of which 137,049 expired shortly thereafter. As at December 31, 2005, 1,191,662 warrants were outstanding, all of which expired, unexercised, in March 2006. No further warrants have been issued to date.

Commitments

The Company has lease agreements for office premises and equipment with estimated minimum annual payments of $363,597 in 2006, $224,097 in 2007 and $73,708 in 2008.

In January 2006, the Company entered into a six month contract with an investor relations firm at a fee of $5,810 per month (US$5,000), plus expenses. The Company may renew the contract under the same terms for an additional six months with prior written notice.

Outlook

The Company completed its review of all non-core properties in March 2006. Six properties, comprised of Inland/Mundare, Bigstone, Viking South, Provost and Brazeau of Alberta and Bayhurst, Saskatchewan, have been packaged and Kobayashi Partners Limited was retained as of April 10, 2006 to conduct a sale of these properties on behalf of the Company. The properties have a value based on the December 31, 2005 engineering report by Sproule Associates Limited of $9.84 million (based on a 10% discounted net present value after Alberta Royalty Tax Credits and before income taxes) as well as an additional land value of $254,355 on 1535.2 net undeveloped hectares as valued by Seaton Jordan & Associates Ltd. effective December 31, 2005. The properties currently produce 200 boe per day of natural gas and natural gas liquids.

Any proceeds contemplated from the sale of the non-core properties will be utilized for debt reduction. Costs for the 2005 fourth quarter exploration program were substantially higher than management anticipated due to unusually robust price increases for the conduct of field operations. Projected cash flow from petroleum products has been revised downward to approximately $9 million for 2006 from the $12 to $15 million previously forecast by management. This is a result of the significant decline in natural gas prices expected for 2006.

The Company's remaining properties will consist of the core areas of Ferrier, Medicine Hat and Jaslan with non-core properties maintained in Mega and Corbett Creek. The reduction in the number of properties will provide the Company's technical team the opportunity to focus on core areas and reduce exploration costs. In Jaslan, approximately 200 boe per day (net) of gas "behind pipe" in four standing gas wells is expected on stream by mid-summer after the installation of compression and pipelines. The net capital cost of the tie-in is expected to be $1.2 million. An additional $1.5 million is budgeted to drill and tie-in four additional wells in Jaslan in the fourth quarter of 2006. Two earning wells will be drilled in Ferrier in the third quarter which will give the Company a 31.875% working interest in the wells plus a 31.875% working interest in 11 sections of land. An additional two Ferrier wells are planned for the fourth quarter on company-owned property. A budget of $3.6 million is anticipated to drill, case, complete and tie these four

wells into company-owned facilities. In addition, third party production volumes are now processed in the 50% owned Ferrier compressor station which will give the Company incremental profit from the Ferrier facility. In Medicine Hat, 20 development locations have been identified, including several farm-in locations which are designed to consolidate the Company's land base in the area. Current plans are to drill 10 wells in the Medicine Hat area in the last half of 2006 with a possibility of increasing that number in the event that natural gas prices improve. The anticipated budget for the drilling, completion and tie-in of these 10 wells is $2.5 million. With two years of shallow gas production history in the Medicine Hat area, the Company is satisfied that the exploration risk is minimal and current fully declined production rates are economic. Current production rates are stable at 700 boe per day, with production growth dependant on drilling success.

Selected Historical Financial Information

2005	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Petroleum and natural gas revenue	1,496,691	1,655,357	1,970,839	3,231,966
Net petroleum and natural gas revenue	951,744	1,063,878	1,306,573	2,211,174
Net income (loss)	(73,331)	(649,962)	322,810	134,136
Net income (loss) per share	–	(0.02)	0.01	–
Funds from (used in) operations	706,244	822,684	1,006,796	1,472,621
Net capital expenditures	1,968,184	2,931,602	1,180,142	4,494,023

2004	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Petroleum and natural gas sales	369,273	780,177	810,029	1,116,081
Net petroleum and natural gas revenue	186,862	382,629	547,635	700,515
Net income (loss)	(110,402)	(219,041)	(439,440)	(22,734)
Net income (loss) per share	(0.01)	(0.01)	(0.02)	–
Funds from (used in) operations	(8,639)	234,126	384,748	223,289
Net capital expenditures	1,649,160	5,525,542	1,903,769	5,354,219

Business Risks and Uncertainties

The Company is exposed to several operational risks inherent in exploring, developing, producing and marketing crude oil and natural gas. These inherent risks include: economic risk of finding and producing reserves at a reasonable cost; financial risk of marketing reserves at an acceptable price given current market conditions; cost of capital risk associated with securing the needed capital to carry out the Company's operations; risk of environment impact and credit risk of non-payment for sales contracts and joint venture partners.

The Company attempts to control operating risks by maintaining a disciplined approach to implementation of its exploration and development programs. Exploration risks are managed by hiring experienced technical professionals and by concentrating the exploration activity on specific core regions that have multi-zone potential where the Company has experience and expertise. The Company also generates internal prospects and participates in projects where ownership interest is considered sufficient to minimize risk. Operational control allows the Company to manage costs, timing and sales of production and to ensure new production is brought on-stream in a timely manner.

The Company maintains a comprehensive insurance program to reduce risk to an acceptable level and to protect it against significant losses. The Company's risk in regards to financial instruments is detailed in note 16 to the annual consolidated financial statements.

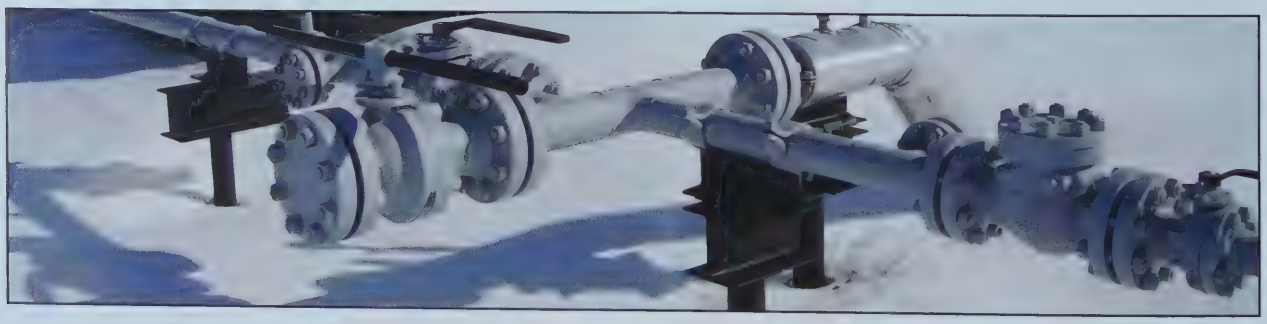
Changes in Accounting Policies

The Canadian Institute of Chartered Accountants (CICA) has issued a number of accounting pronouncements, some of which may impact the Company's reported results and financial position in future periods.

Comprehensive Income/Financial Instruments/Hedges

The CICA issued new standards in early 2005 for Comprehensive Income (CICA 1530), Financial Instruments (CICA 3855) and Hedges (CICA 3865), which will be effective for the reporting year-end 2007. The new standards will bring Canadian rules in line with current rules in the US. The standards will introduce the concept of "Comprehensive Income" to Canadian GAAP and will require that an enterprise (a) classify items of comprehensive income by their nature in a financial statement and (b) display the accumulated balance of comprehensive income separately from retained earnings and additional paid-in capital in the equity section of a statement of financial position. Derivative contracts will be carried on the balance sheet at their mark-to-market value, with the change in value flowing to either net income or comprehensive income. Gains and losses on instruments that are identified as hedges will flow initially to comprehensive income and be brought into net income at the time the underlying hedged item is settled. It is expected that this standard will be effective for the Company's 2007 reporting. Any instruments that do not qualify for hedge accounting will be marked-to-market with the adjustment (tax effected) flowing through the income statement.

The Company does not currently have any hedges in place that carry into 2006 or 2007 so there would not be any impact based on the current position.



Disclosure Controls and Procedures

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Company is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure. The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by the annual filings, that the Company's disclosure controls and procedures as of the end of such period are effective to provide reasonable assurance that material information related to the Company, including its consolidated subsidiaries, is made known to them by others within those entities. It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

CORPORATE INFORMATION

BOARD OF DIRECTORS

James G. Evaskevich
Robert Weir
Gordon Bowerman[1]
Douglas Stuve [1]
Joseph Dutton[1]

[1] Audit and Reserves Committee

EXECUTIVE OFFICERS

James G. Evaskevich, President & CEO
Penny Payne, CFO
Robert Weir, VP Engineering
Donald Poruchny, VP Exploration

SOLICITER

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#1600, 333 – 7 Avenue S.W.
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AUDITORS

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Calgary, AB T2P 3E8

TRANSFER AGENT

Computershare
Calgary, AB

EVALUATION ENGINEERS

Sproule Associates Limited
Calgary, AB

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STOCK EXCHANGE LISTING

Toronto Venture Exchange
Trading Symbol "YAN"

Abbreviations

mbbls – thousands of barrels
mmcf – million cubic feet
Mmcf/d – million cubic feet per day
boe – barrels of oil equivalent
NGLS – natural gas liquids, consisting of any one or more propane, butane or condensate
boe/d – barrels of oil equivalent per day
bbls - barrels
bbls/d – barrels per day
mbbls – thousands of barrels
MMBTU – million British thermal units

Conversions: All conversions converting natural gas to crude oil equivalent have been made using a ratio of six mcf natural gas to one barrel of crude oil equivalent

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